

State of Idaho

Legislative Services Office

Management Report

A communication to the Joint Finance-Appropriations Committee

TAX COMMISSION

FY 2006, 2007, and 2008

Report IC35208
Date Issued: January 19, 2010

Serving Idaho's Citizen Legislature



Don H. Berg, Manager

Idaho Legislative Services Office
Legislative Audits Division

TAX COMMISSION

SUMMARY

PURPOSE OF MANAGEMENT REVIEW

We conducted a management review of the Tax Commission covering the fiscal years ended June 30, 2006, 2007, and 2008. Our review covered general administrative procedures and accounting controls to determine that activities are properly recorded and reported.

The intent of this review was not to express an opinion, but to provide general assurance on internal controls and to raise the awareness of management and others of any conditions and control weaknesses that may exist and offer recommendations for improvement.

CONCLUSION

Our review disclosed no internal control weaknesses in the general accounting controls of the Commission. However, our review of the taxpayer protest resolution process identified a weakness in the use of summons.

FINDINGS AND RECOMMENDATIONS

This report contains one finding and recommendation.

1. The summons process is not used in all cases where taxpayers fail to provide evidence for audit purposes.

The complete finding is detailed on page 1.

A copy of this report is available at <http://www.legislature.idaho.gov/audit> or by calling 208-334-4832.

PRIOR FINDINGS AND RECOMMENDATIONS

There were no findings and recommendations in the prior report.

AGENCY RESPONSE

The Commission has reviewed the report and is in general agreement with its contents.

FINANCIAL INFORMATION

The Commission fulfills its legal and administrative duties with funds primarily received from the State General Fund. Other sources of administrative funds include motor fuel taxes, multi-state taxes, and abandoned property receipts. The following financial data is for informational purposes only.

TAX COMMISSION – FISCAL YEAR 2008

Fund	Fund Name	Beginning Cash Balance/ Appropriation	Receipts/ Transfers-in	Expenditures/ Transfers-out	Ending Cash Balance/ Appropriation
0001	General Fund ¹	\$27,584,081	\$7,246	\$27,500,983	\$90,344
0150	Budget Stabilization ²	22,721	0	6,221	16,500
0276	Multi-State Tax ³	221,357	11,885,337	11,876,763	229,931
0338	Administration Funds ⁴	933,457	3,811,500	3,784,266	960,691
0348	Federal Grant	4,763	77,000	81,763	0
0401	Seminars and Publications	57,526	145,969	144,743	58,752
0518	Abandoned Property	250,000	12,897,169	12,897,169	250,000

¹Beginning balance includes encumbrances of \$120,706; ending balance includes encumbrances of \$89,998.

²Beginning and ending balance includes encumbrances of \$16,500.

³Beginning balance includes encumbrances of \$75,327.

⁴Beginning balance includes encumbrances of \$15,223; ending balance includes encumbrances of \$1,765.

The Commission collected nearly \$3.6 billion in tax revenue in fiscal year 2008. Of this amount, nearly \$2.7 billion was deposited in the General Fund, and \$396 million was returned as refunds. The remaining money was allocated and distributed to other funds to be used for specific purposes. The receipts and distributions are summarized in the following schedule.

Tax Commission
Receipts and Distribution Summary – Fiscal Year 2008

<u>Tax Type</u>	<u>Receipts</u>	<u>Fund</u>	<u>Distributions</u>
Individual Income Tax	\$1,705,036,185	General Fund	\$2,698,412,350
Corporate Income Tax	212,879,756	Fish and Game Donation	54,298
Sales Tax	1,339,278,004	Abandoned Mine Reclaim Fund	1,300,705
Cigarette Tax	46,216,367	Petroleum Storage Trust	1,398,476
Tobacco Tax	8,349,574	Budget Stabilization Fund	0
Beer Tax	4,587,618	Cancer Control	374,957
Wine Tax	3,133,625	Central Tumor Registry	149,980
Kilowatt Hour Tax	1,599,181	Alcohol Intoxification Treatment	1,287,279
Mine License Tax	3,829,532	Juvenile Justice	4,821,625
Estate Tax	32,204	Water Pollution Control	4,800,000
Abandoned Property	12,882,634	Travel and Convention	7,255,551
Motor Fuel Tax	238,280,049	Parks and Recreation	4,791,314
Boise Auditorium District Tax	4,311,970	Search and Rescue	41,238
Idaho Travel and Convention Tax	7,378,675	Multi-State Tax Compact	1,871,623
Suspense Fund	83,921	Custodial Funds Administration	248,400
Local Option Tax	3,323,349	Motor Fuel Tax Administration	3,563,100
Miscellaneous Revenue and Taxes	265,033	Wine Shipper Fee (ISP)	3,225
Total	<u>\$3,591,467,677</u>	Miscellaneous Income	145,969
		Permanent Building Fund	43,804,105
		Public Schools	5,495,211
		Children's Trust Donation	85,092
		Sales Tax Distributions	167,983,755
		Agriculture Property Tax Relief	8,487,103
		Sales Tax Pilot Project Fund	932,755
		County Inheritance Tax	3,220
		Refunds	396,304,244
		Abandoned Property Trust	7,225,465
		Election Campaign Fund	35,631
		Suspense Fund	160,588
		Idaho Transportation Department	222,745,631
		Non-State Funds in Trust	7,684,786
		Total	<u>\$3,591,467,676</u>

OTHER INFORMATION

We discussed other issues which, if changed, would improve internal control, compliance, and efficiency.

This report is intended solely for the information and use of the State of Idaho and the Tax Commission and is not intended to be used by anyone other than these specified parties.

We appreciate the cooperation and assistance given to us by the Tax Commission chairman, Royce Chigbrow, and his staff.

ASSIGNED STAFF

Chris Farnsworth, CPA, Managing Auditor

Jim Combo, CPA, In-Charge Auditor

Mark Schoenfeld, Staff Auditor

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FINDINGS AND RECOMMENDATIONS

FINDING 1

1. The summons process is not used in all cases where taxpayers fail to provide evidence for audit purposes.

Idaho Code, Section 63-3042 authorizes the Commission to summon witnesses and documents relating to any matter within its jurisdiction. The Commission uses the summons process infrequently to obtain requested evidence necessary to determine tax amounts due.

We reviewed five multi-state business income tax protest cases and identified two where the taxpayer failed to furnish the requested evidence during the audit. The summons process was not used for these two cases and the compromise and resolution of the issues were made without the requested evidence. Memos in the files stated that the lack of information would make these cases difficult to defend in court should the taxpayer appeal the decision, but the reasons for not using the summons process were not identified or documented. Although the summons process can be lengthy and time-consuming, the quality and content of evidence is essential to the audit process and resolution of the issues.

We also noted that guidance from the Commission's legal staff is not always requested or documented in the audit files, and some concerns were raised by legal staff that assisting the audit staff could affect their independence during the negotiation process between the Commissioners and taxpayers. Communication and support between the legal and audit staffs is also essential to the audit and resolution process.

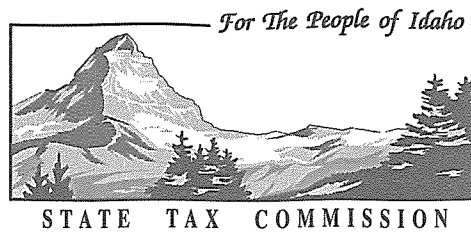
RECOMMENDATION

We recommend that the Commission establish guidelines for the audit staff to request and document guidance from the Commission's legal staff in situations where the taxpayer fails to provide requested evidence. This documentation should include the reasons for not using the summons process. We also recommend that the Commission develop procedures for the legal staff to provide guidance to the audit staff without creating an independence issue on protest cases.

AGENCY'S CORRECTIVE ACTION PLAN

The Commission's attorneys work with the income tax audit staff to improve the instructions in the audit manual for identifying proper cases for the use of a summons and the proper procedures for preparing and serving them. Those instructions will continue to be regularly and jointly reviewed and improved to include further direction on the type of documentation needed when the summons process is not used. Whether to use a summons in a particular case remains a case-by-case judgmental determination. Attorneys will be available to assist both in the decision about whether to issue a summons and in the preparation and proper service of a summons.

AGENCY RESPONSE



800 Park Blvd., Plaza IV • Boise, ID • 83722

December 21, 2009

Legislative Audits Division
c/o James Combo, Auditor
Statehouse, P.O. Box 83720
Boise, Idaho 83720-0054

Re: Tax Commission Response to Audit Finding

Dear Mr. Combo:

Please include the following as the ISTC response to the finding:

We appreciate the audit comments and are in agreement.

The commission's attorneys work with the income tax audit staff to improve the instructions in the audit manual for identifying proper cases for the use of a summons and the proper procedures for preparing and serving them. Those instructions will continue to be regularly and jointly reviewed and improved, to include further direction on the type of documentation needed when the summons process is not used. Whether to use a summons in a particular case remains a case-by-case judgmental determination. Attorneys will be available to assist both in the decision about whether to issue a summons and in the preparation and proper service of a summons.

Thank you for your comments.

Sincerely,

A handwritten signature in black ink, which appears to read "Royce C. Chigbrow", is written over the typed name and title. The signature is fluid and cursive.

Royce C. Chigbrow
Chairman

rcc/mp/vjd

APPENDIX

HISTORY

The Idaho State Legislature created the first Board of Tax Commissioners, known as the Idaho State Tax Commission. Members of the Idaho Public Utilities Commission comprised the first Idaho State Tax Commission. They served as ex-officio tax commissioners and received no additional salary or compensation. The principal duty of the original State Tax Commission was to coordinate assessment efforts for various county assessors; however, they had no powers with respect to meeting as a State Board of Equalization. The original State Tax Commission was dissolved by the Idaho Legislature in 1915.

In 1945, the Constitution was amended to provide for a State Tax Commission consisting of four members, not more than two of whom could belong to the same political party. These members were appointed by the Governor for staggered six-year terms, subject to approval by the Idaho State Senate.

At this time, all duties previously imposed on the State Board of Equalization by the Constitution and laws of the State were transferred to the newly created State Tax Commission. This Commission was a part-time Commission, and members were paid a per diem for each day devoted to the performance of Commission duties. In no event was the full performance of duties to require more than 100 days of service in any one year. The Commission employed the full-time services of an executive officer, who also acted as secretary to the Commission.

In 1967, the Idaho Legislature abolished the Office of the Tax Collector, the office primarily responsible for collecting various taxes, including individual and corporate income tax, gasoline tax, sales tax, and other miscellaneous taxes. At that time, the legislature also changed the services of the State Tax Commission from part-time to full-time. This full-time Commission also assumed all duties and responsibilities of the former Office of the Tax Collector.

Effective July 1, 1974, State government reorganization combined the State Tax Commission and the State Board of Tax Appeals into the presently organized Department of Revenue and Taxation, in concept only. That is, the Board of Tax Appeals is not physically located within the State Tax Commission, and the State Tax Commission exercises no administrative or functional authority over the Board of Tax Appeals.

STATUTORY AUTHORITY

In addition to the constitutional powers conferred upon the Department of Revenue and Taxation by Article VII of the Idaho Constitution, the Department derives other specific duties, responsibilities, and authorities from Idaho Code, Title 63. Some of the more comprehensive general duties and responsibilities are:

1. To exercise general supervision over the system of ad valorem taxation throughout the State.
2. To assess taxation for all Class-3 (operating) properties.
3. To conduct annual sales ratio studies for real property throughout the State for the purpose of allocating school funds.

4. To administer, assess, collect, audit, and enforce taxes on income, sales, cigarettes, beer, gasoline, wine, kilowatt hour, mine license, inheritance, unclaimed property, and ad valorem taxes on car companies with assessed values of less than \$500,000.
5. To publish rules and regulations pertaining to sales, income, miscellaneous and ad valorem laws, and to evaluate procedures.
6. To provide educational programs and an appraisal school for Department employees and county assessors and their staff members.
7. To maintain a tax research section to observe and investigate the effectiveness and adequacy of the revenue laws of the State, and to assist the executive and legislative departments in estimation of revenue, analysis of tax measures, and determination of the administrative feasibility of proposed tax legislation.

ORGANIZATIONAL STRUCTURE

The organizational structure of the present Department is illustrated by the chart following this appendix. Total personnel employed by the Department in fiscal year 2008 was 413.5. The Department is organized into four divisions, plus a tax policy section and legal section. Within the Audit Collections Division are five field offices located in Coeur d'Alene, Idaho Falls, Lewiston, Pocatello, and Twin Falls.

FUNDING

General Fund (0001)

Sources – The General Fund consists of "moneys received into the treasury and not specially appropriated to any other fund" (I.C. § 67-1205). Fund sources are: individual income tax, corporate income tax, sales tax, cigarette tax, beer tax, wine tax, liquor surcharge, kilowatt hour tax, mine license tax, interest on investments of certain idle State funds, court fees and fines, insurance premium tax, sale of alcoholic beverage licenses, filing of articles of incorporation and other fees collected by the Secretary of State, unclaimed property, and other miscellaneous sources from various agency receipts.

Uses – The Department receives a General Fund appropriation used for personnel costs, operating expenditures, and capital outlay for the operation of the Department.

Economic Recovery Reserve Fund (0150-01)

Sources – Moneys in the fund are from cigarette taxes (deposits made pursuant to I.C. § 63-2520) and interest earnings from the investment of idle moneys in the fund. Although not specified in law, it also includes transfers from the General Fund or other funds as approved by the legislature (I.C. § 67-3520).

Uses – The fund was created for the purpose of meeting General Fund revenue shortfalls, meeting expenses incurred as the result of a major disaster declared by the Governor, or for providing one-time tax relief payments to the citizens of Idaho. It has been used for the 27th pay period in fiscal year 2006, one-time replacement equipment costs, economic development projects, the Parks and Recreation "Experience Idaho" initiative, and other line-items as approved by the legislature (I.C. § 67-3520).

Motor Fuels Distribution Fund (0267)

Sources – This fund was created in fiscal year 1998, as a suspense fund to receive motor fuel tax receipts. All motor fuel taxes are deposited in this fund, and it also receives interest earned on the fund balance.

Uses – After the fuel tax returns are processed and the amount of each tax type is determined, the money is distributed to the appropriate funds based on Idaho Code requirements. (See the tax description and distribution requirements for fuel taxes in the previous section.)

Multistate Tax Compact Fund (0276)

Sources – Money collected as a direct result of audits made by the Multistate Tax Commission (on behalf of the State of Idaho) is paid by the State Tax Commission into the Multistate Tax Compact Fund. The Multistate Tax Compact Fund was formed to determine the tax liability of multistate taxpayers, promote uniformity or compatibility in tax systems, facilitate taxpayer convenience and compliance in filing tax returns, and avoid duplicate taxation across states (I.C. § 63-3709).

Uses – The State Tax Commission receives the budget for the Multistate Tax Commission, including a statement of Idaho's share. Annually, on or before February 1, the Tax Commission certifies to the Joint Finance-Appropriations Committee, the Senate Local Government and Taxation Committee, and the House Revenue and Taxation Committee whether the budget complies with the Multistate Tax Compact. Unless the legislature determines otherwise, the amounts which the State Tax Commission has certified as complying are appropriated from the Multistate Tax Compact Fund to the Multistate Tax Commission.

If the funds in the Multistate Tax Compact Fund exceed 110% of the most recent annual appropriation made to the Multistate Tax Commission, the excess is transferred to the State General Fund.

Payments to the Multistate Tax Commission from the Multistate Tax Compact Fund are made only on approval of the State Tax Commission (I.C. § 63-3709).

Administration and Accounting Fund (0338-01)

Sources – The State Tax Commission is directed to retain funds to cover its cost of collecting and administering certain trust funds. For the following trust funds the amount is \$3,000 or 20%, whichever is less:

1. The Fish and Game Trust Fund (0051)
2. The Children's Trust Fund (0483)

For other taxes, the State Tax Commission is authorized to retain an amount of money equal to the cost of collection and administration (not to exceed legislative appropriation). Those taxes are:

1. Idaho Travel and Convention Tax (0212)
2. Greater Boise Auditorium District (0630)
3. Petroleum Clean Water Trust Fund (0130)

Uses – Funds in the Administration and Accounting Fund are used to defray the cost of collecting and administering the taxes of the trust funds noted above (I.C. §§ 63-3067, 67-4718, 63-4209, and 41-4909).

Administration and Accounting Services to Transportation Fund (0338-02)

Sources – Gasoline tax receipts equal to the cost of collecting, administering, and enforcing the gasoline tax requirements, not to exceed the amount appropriated (I.C. § 63-2412(a)).

Special fuels tax receipts equal to the cost of collecting, administering, and enforcing the Special Fuels Tax, not to exceed the amount appropriated (I.C. § 63-2418(1)).

Uses – The funds are used to pay the costs of administering, collecting, auditing, and enforcing the laws related to the Gasoline Tax and Special Fuels Tax programs (I.C. §§ 63-2412 through 63-2418).

Federal Grant Fund (0348)

Sources – Federal government.

Uses – To enforce compliance of highway motor fuel use tax.

Seminars and Publications Fund (0401)

Sources – Various sources, including fees, educational-related sales, tax regulations and printed materials, copy charges, supplies, bad-check charges, postage reimbursement, sale of maps, and unclaimed property lists. All sales are primarily made to the public.

Uses – These funds are used to defray costs associated with collecting and administering these funds.

Abandoned Property Trust – Unclaimed Property Fund (0518-01).

Sources – Receipts from (1) any deposits, together with interest and purchase of shares made in Idaho with a banking or financial organization that has been inactive for seven years; (2) unclaimed funds that are owned and unpaid by life insurance companies for five years; (3) deposits and refunds payable by utilities for more than five years; and (4) certain other abandoned and inactive funds.

The State Tax Commission is required to maintain a record of the name and last known address of each person thought to own the property and to make the record available for public inspection (I.C. § 14-523).

Uses – All funds are appropriated to the State Tax Commission to meet the costs necessary to carry out and enforce the law. Funds are used for payment of claims, refunds, appraisal costs, property acquisition, advertising, and any estate taxes due to the State by the claimant.

Each month the Commission transfers all funds in excess of \$250,000 to the State General Fund (I.C. § 14-523).

OTHER FUNDS

The Department uses several additional funds to carry out its legal and administrative duties. These funds are used to make legally required refunds and allocations, and to transfer tax revenue to the appropriate fund or entity as explained below.

Tax Commission Refund Fund (0516)

Sources – Twenty percent (20%) of State individual and corporate income taxes is deposited in the State Refund Fund (I.C. § 63-3067).

Additionally, as necessary, an amount sufficient to pay refunds for various tax types is distributed to this fund from the following taxes:

1. Sales Tax
2. Cigarette Tax
3. Beer Tax
4. Gasoline Tax
5. Estate Tax
6. Wine Tax
7. Kilowatt Hour Tax
8. Mine License Tax
9. Tobacco Tax
10. Special Fuels Tax
11. Travel and Convention Tax
12. Boise Auditorium Tax
13. Illegal Drug Tax
14. Nez Perce County Sales Tax

Uses – The State Refund Fund repays overpayments and any other erroneous receipts illegally assessed or collected. When necessary, for the purpose of making prompt refund payments, the State Tax Commission may request that the Board of Examiners authorize transferring an additional specific amount from the income tax collections to the State Refund Fund. Any unencumbered balance over \$1.5 million in the fund on June 30 is transferred to the State General Fund (I.C. § 63-3067).

Revenue Sharing Fund (0502-01)

Sources – This fund receives 11.5% of the State sales tax revenue (I.C. § 63-3638).

Uses – This tax is distributed to cities and counties as follows:

1. 28.2% to various cities, distributed as follows:
 - a. 50% to cities in the proportion that each city's population bears to the population of all cities within the State.
 - b. 50% to the cities in the proportion that their preceding year's assessed market value bears to the assessment value of all cities within the State.
2. 28.2% to various counties as follows:
 - a. \$1,320,000 split equally between each county in the State.
 - b. The balance to the counties in the proportion that the population of each county bears to the population of the State.
3. 35.9% to various counties as follows:
 - a. Each county that received a payment under the provisions of I.C. § 63-3638(e) during the fourth quarter of 1999, shall be entitled to a like amount. If that amount is more or less than the fourth quarter payment, the payment will be reduced or increased proportionately not to exceed 105% of the total payment made in the fourth quarter of 1999. Any amount exceeding 105% of the fourth quarter amount of 1999, shall be split 50% between cities and counties, and shall be distributed based on population percentages.

4. 7.7% is various special taxing districts as follows:
- a. Each district that received a payment under the provisions of I.C. § 63-3638 (e) during the fourth quarter of 1999, shall be entitled to a like amount during succeeding calendar quarters. If revenues are not equal to those distributed in the fourth quarter of 1999, each special taxing district's payment shall be reduced proportionately. If the revenues exceed those of the fourth quarter payment of 1999, the excess shall be distributed based on the proportion that each districts' current property tax budget bears to the sum of current property tax budgets of all such districts in the State.
 - b. If a special purpose taxing district is dissolved or disincorporated, the State Tax Commission shall continuously distribute to the board of county commissioners, an amount equal to the last quarter's distribution prior to dissolution or disincorporation. The board shall determine any redistribution of the money received.

County Circuit Breaker Fund (0502-03)

Sources – This fund receives State sales tax revenue in the amount certified to the county auditor under the circuit breaker provisions of the Idaho Code (I.C. § 63-709).

Uses – Each year the State Tax Commission reviews the claims and certifies the dollar amount to the county auditor by the third Monday in November. By December 20, the State Tax Commission pays each county one-half the amount due, with the second half paid by the following June 20 (I.C. §§ 63-701 through 63-710).

Sales Tax Ag Property Tax Relief (0502-06)

Sources – Funded by sales tax revenues (I.C. § 63-3638(10)).

Uses – Provides payments to counties and other taxing districts to replace property tax revenue lost when agricultural equipment was exempted from property taxes (I.C. § 63-602EE).

Demonstration Pilot Project (0502-08)

Sources – 60% of the sales tax collected by certain qualified retailers (I.C. § 63-3641).

Uses – Reimbursement of developers for costs related to approved transportation improvements, not to exceed \$35 million for a single improvement (I.C. § 40-109).

Estate Tax Fund (0507)

Sources – The Commission collects estate taxes and remits the money to the State Treasurer (I.C. § 14-413).

Uses – Estate taxes are distributed as follows:

1. 10% to a fund for distribution to counties, at least quarterly.
2. An amount sufficient to pay current refund claims to the State Refund Fund.
3. The balance to the General Fund.

Election Campaign Fund (0600)

Sources – Taxpayers filing individual income tax returns, whose income tax liability is at least \$1, may designate \$1 to be paid to the Election Campaign Fund (I.C. § 63-3088).

Uses – Funds are disbursed monthly to the State Controller's Office for distribution to Idaho's various political parties.

Custodial Fund (0630)

Sources – Suspense items are charged to this fund until they are ready to be credited to the proper fund. This includes items like electronic fund transfers and field office deposits. Several Idaho Code sections require the State to bond taxpayers. All bonds are receipted in this fund and a subsidiary journal of individual bonds is maintained.

Uses – Suspense items are held in this fund until they are identified and can be charged to the proper fund. The bond amounts are held as long as required.

Non-State Funds in Trust (0630-02)

Sources – Local option tax receipts, Boise Auditorium District tax receipts, and a portion of wine tax receipts are deposited into this fund.

Uses – Receipts are distributed monthly as follows:

1. Local option taxes are distributed to Nez Perce County.
2. Wine tax receipts are distributed to the Idaho Grape Growers and Wine Producers Commission.
3. Boise Auditorium District tax receipts are distributed to the Boise Auditorium District.

State Tax Commission

